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December 2013

# FINANCIAL AUDIT

## Bureau of the Fiscal Service's Fiscal Years 2013 and 2012 Schedules of Federal Debt

## Why GAO Did This Study

GAO is required to audit the consolidated financial statements of the U.S. government. Because of the significance of the federal debt held by the public to the government-wide financial statements, GAO audits Fiscal Service's Schedules of Federal Debt annually to determine whether, in all material respects, (1) the schedules are reliable and (2) Fiscal Service management maintained effective internal control over financial reporting relevant to the Schedule of Federal Debt. Further, GAO tests compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements related to the Schedule of Federal Debt.

Federal debt managed by Fiscal Service consists of Treasury securities held by the public and by certain federal government accounts, referred to as intragovernmental debt holdings. Debt held by the public essentially represents the amount the federal government has borrowed to finance cumulative cash deficits. Intragovernmental debt holdings represent balances of Treasury securities held by federal government accounts—primarily federal trust funds such as Social Security and Medicare—that typically have an obligation to invest their excess annual receipts (including interest earnings) over disbursements in federal securities.

In commenting on a draft of this report, Fiscal Service's Commissioner concurred with GAO's conclusions.

View [GAO-14-173](#). For more information, contact Gary T. Engel at (202) 512-3406 or [engelg@gao.gov](mailto:engelg@gao.gov).

## FINANCIAL AUDIT

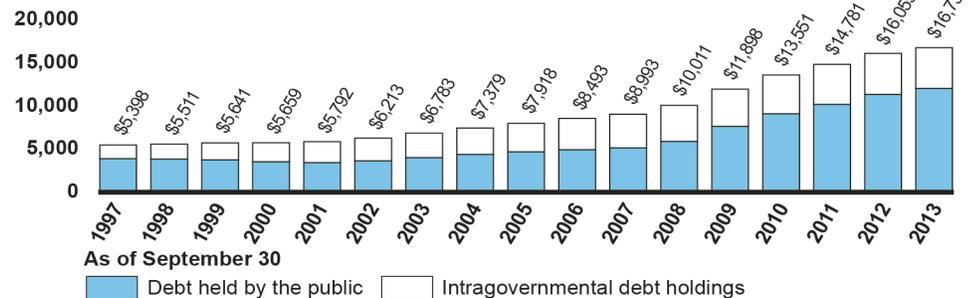
### Bureau of the Fiscal Service's Fiscal Years 2013 and 2012 Schedules of Federal Debt

## What GAO Found

In GAO's opinion, the Bureau of the Fiscal Service's (Fiscal Service) Schedules of Federal Debt for fiscal years 2013 and 2012 were fairly presented in all material respects, and although information systems controls could be improved, Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2013. GAO's tests disclosed no instances of reportable noncompliance for fiscal year 2013 with selected provisions of applicable laws, regulations, contracts, and grant agreements related to the Schedule of Federal Debt.

Total federal debt managed by Fiscal Service has increased by 210 percent and the debt limit has been raised 14 times, from \$5,950 billion to \$16,699 billion, from fiscal year 1997, the first year of audit, through September 30, 2013.

**Total Federal Debt Outstanding, September 30, 1997, through September 30, 2013**  
Dollars in billions



Note: A small amount of total federal debt is not subject to the debt limit.  
Source: Fiscal Service.

Due to delays in raising the debt limit, during fiscal year 2013, the Department of the Treasury (Treasury) twice, and for almost half of the fiscal year, deviated from its normal debt management operations and took a number of extraordinary actions—consistent with relevant laws and regulations—to avoid exceeding the debt limit. Many extraordinary actions taken by Treasury during fiscal year 2013 resulted in federal debt securities not being issued to certain federal government accounts. Consequently, the resulting uninvested principal as of September 30, 2013, totaling \$248 billion, and related interest totaling \$801 million, are not reported on the fiscal year 2013 Schedule of Federal Debt. Uninvested principal was subsequently restored to affected federal government accounts, increasing the federal debt. As GAO has previously reported, delays in raising the debt limit can create uncertainty in the Treasury market and lead to higher Treasury borrowing costs. To avoid such uncertainty and related borrowing costs, GAO noted, in its February 2011 and July 2012 reports related to the debt limit, that Congress should consider ways to better link decisions about the debt limit with decisions about spending and revenue to avoid potential disruptions to the Treasury market and to help inform the fiscal policy debate in a timely way. As decision makers determine funding for the federal government's operations in the short term over the next few months and as they decide how to address the federal government's long-term fiscal challenges, it will be important at the time such decisions are made that consideration be given as to the impact the decisions will have on the level of federal debt.

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## Abbreviations

BBEDCA	Balanced Budget and Emergency Deficit Control Act
FMFIA	Federal Managers' Financial Integrity Act
GDP	gross domestic product

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December 12, 2013

The Honorable Jacob J. Lew  
Secretary of the Treasury

Dear Mr. Secretary:

The accompanying independent auditor's report presents the results of our audits of the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service (Schedule of Federal Debt) for the fiscal years ended September 30, 2013, and 2012. The Schedules of Federal Debt present the beginning balances, increases and decreases, and ending balances for (1) Federal Debt Held by the Public and Intragovernmental Debt Holdings, (2) the related Accrued Interest Payables, and (3) the related Net Unamortized Premiums and Discounts managed by the Department of the Treasury's (Treasury) Bureau of the Fiscal Service (Fiscal Service), and include accompanying notes.

The independent auditor's report contains (1) our unmodified opinions on the Schedules of Federal Debt for the fiscal years ended September 30, 2013, and 2012; (2) our opinion that although internal controls could be improved, Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2013; and (3) the results of our tests of Fiscal Service's compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements related to the Schedule of Federal Debt, which identified no instances of reportable noncompliance. The report also discusses deficiencies that we identified in information system controls that collectively represent a significant deficiency in internal control over financial reporting relevant to the Schedule of Federal Debt.<sup>1</sup>

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<sup>1</sup>A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

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As of September 30, 2013, and 2012, federal debt managed by Fiscal Service totaled \$16,732 billion and \$16,059 billion, respectively, primarily for borrowings to fund the federal government's operations. As shown on the Schedules of Federal Debt, these balances consisted of approximately (1) \$11,976 billion as of September 30, 2013, and \$11,270 billion as of September 30, 2012, of debt held by the public and (2) \$4,756 billion as of September 30, 2013, and \$4,789 billion as of September 30, 2012, of intragovernmental debt holdings.

Debt held by the public essentially represents the amount the federal government has borrowed from the public to finance cumulative cash deficits. When a cash surplus occurs, the annual excess funds can be used to reduce debt held by the public. In other words, annual cash deficits or surpluses generally approximate the annual net change in the amount of federal government borrowing from the public. Debt held by the public represents federal debt issued by Treasury and held by investors outside of the federal government, including individuals, corporations, state or local governments, the Federal Reserve, and foreign governments. The majority of debt held by the public consists of marketable Treasury securities, such as bills, notes, bonds, and Treasury Inflation-Protected Securities that are sold through auctions and can be resold by whoever owns them. Treasury also issues a smaller amount of nonmarketable securities, such as savings securities and State and Local Government Series securities.

As we have noted in previous years, Treasury reporting shows that foreign ownership of Treasury securities represents a significant portion of debt held by the public.<sup>2</sup> As of June 30, 2013, the reported amount of Treasury securities held by foreign and international investors represented an estimated 47 percent of debt held by the public. This percentage is slightly lower than the 48 percent as of June 30, 2012, but remains considerably higher than the estimated 30 percent of debt held by the public as of June 30, 2001. Treasury estimates that the amount of Treasury securities held by foreign and international investors has increased from \$983 billion as of June 30, 2001, to \$5,594 billion as of June 30, 2013—an increase of \$4,611 billion. Estimates of foreign ownership of Treasury securities are derived from information reported

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<sup>2</sup>GAO, *Financial Audit: Bureau of the Public Debt's Fiscal Years 2012 and 2011 Schedules of Federal Debt*, [GAO-13-114](#) (Washington, D.C.: Nov. 8, 2012).

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under the Treasury International Capital reporting system, not from the financial system used to prepare the Schedule of Federal Debt. These estimates are not reported on the Schedules of Federal Debt and, as such, we do not audit these amounts.<sup>3</sup>

Intragovernmental debt holdings represent federal debt owed by Treasury to federal government accounts—primarily federal trust funds such as Social Security and Medicare—that typically have an obligation to invest in federal securities their excess annual receipts (including interest earnings) over disbursements. Most federal government accounts invest in special nonmarketable Treasury securities that represent legal obligations of the Treasury and are guaranteed for principal and interest by the full faith and credit of the U.S. government. The federal government uses the federal government accounts' invested cash surpluses to assist in funding other federal government operations. Unlike debt held by the public, intragovernmental debt holdings are not shown as balances on the federal government's consolidated financial statements because they represent loans from one part of the federal government to another. Under U.S. generally accepted accounting principles, when the federal government's financial statements are consolidated, those offsetting balances are eliminated.

Debt held by the public and intragovernmental debt holdings are very different. Debt held by the public represents a claim on today's taxpayers and absorbs resources from today's economy. In addition, the interest paid on this debt may reduce budget flexibility because, unlike most of the budget, it cannot be controlled directly. In contrast, intragovernmental debt holdings reflect a claim on taxpayers and the economy in the future. Specifically, when federal government accounts redeem Treasury securities to obtain cash to fund expenditures, Treasury usually borrows from the public to finance these redemptions.<sup>4</sup>

We have audited the Schedule of Federal Debt since fiscal year 1997. Over this period, total federal debt has increased by 210 percent. Also

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<sup>3</sup>Department of the Treasury, *Major Foreign Holders of Treasury Securities*, accessed December 4, 2013, <http://www.treasury.gov/resource-center/data-chart-center/tic/Documents/mfh.txt>.

<sup>4</sup>For more information regarding the federal debt, see GAO, *Federal Debt: Answers to Frequently Asked Questions*, accessed December 4, 2013, [www.gao.gov/special.pubs/longterm/debt](http://www.gao.gov/special.pubs/longterm/debt).

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during this period, the statutory debt limit was raised 14 times, from \$5,950 billion to \$16,699 billion.<sup>5</sup> During the last 4 fiscal years, total federal debt has increased by \$4,834 billion, or 41 percent, from \$11,898 billion as of September 30, 2009, to \$16,732 billion as of September 30, 2013. Of the total increase, \$4,424 billion was from the increase in debt held by the public and \$410 billion was from the increase in intragovernmental debt holdings. The economic downturn along with the federal government's response to it contributed to the rapid buildup in debt held by the public. During fiscal year 2013, total federal debt increased by a net \$673 billion, consisting of a (1) \$706 billion increase in debt held by the public and (2) \$33 billion decrease in intragovernmental debt holdings. This decrease in intragovernmental debt holdings resulted from certain extraordinary actions taken by Treasury consistent with relevant laws and regulations to manage federal debt to avoid exceeding the debt limit.<sup>6</sup> Although federal debt continued to increase in fiscal year 2013, the increase in debt held by the public was significantly lower than the fiscal year 2012 increase of \$1,143 billion. Notably, while the statutory debt limit was raised on six different occasions during the last 4 fiscal years, increasing by about 38 percent, from \$12,104 billion to \$16,699 billion, delays in raising the debt limit occurred in each of the last 3 fiscal years. Delays result in Treasury deviating from its normal debt management operations and taking a number of extraordinary actions within its legal authorities to avoid exceeding the debt limit.

During fiscal year 2013, Treasury twice, and for almost half of the fiscal year, faced the challenge of managing federal debt close to the statutory debt limit. The first delay in raising the debt limit occurred from December 31, 2012, through February 3, 2013, with Treasury taking a number of extraordinary actions consistent with relevant laws and regulations to avoid exceeding the debt limit. These actions included suspending investments to certain federal government accounts. On February 4, 2013, the No Budget, No Pay Act of 2013 was enacted, which suspended the statutory debt limit through May 18, 2013.<sup>7</sup>

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<sup>5</sup>A small amount of total federal debt reported on the Schedule of Federal Debt is not subject to the debt limit. This amount is primarily composed of unamortized discounts on Treasury bills and Zero Coupon Treasury bonds.

<sup>6</sup>Actions that are not part of Treasury's normal cash and debt management operations are considered "extraordinary actions" by Treasury.

<sup>7</sup>Pub. L. No. 113-3, § 2, 127 Stat. 51 (Feb. 4, 2013).

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Subsequent to the start of the suspension period, Treasury restored principal and interest to the affected federal government accounts in accordance with relevant laws. An increase in the debt limit was not enacted before the suspension period ended and therefore, consistent with the No Budget, No Pay Act of 2013, the debt limit was raised on May 19, 2013, to the amount of qualifying federal debt securities outstanding at that date, or \$16,699 billion. As such, a second delay in raising the debt limit occurred with Treasury again taking certain extraordinary actions consistent with relevant laws and regulations to avoid exceeding the limit from May 20, 2013, through October 16, 2013. On October 17, 2013, the Continuing Appropriations Act, 2014 was enacted, which suspended the statutory debt limit through February 7, 2014.<sup>8</sup> If an increase in the debt limit is not enacted before the end of this suspension period, consistent with the Continuing Appropriations Act, 2014, the debt limit will be increased by the change in qualifying federal debt securities outstanding on October 17, 2013, compared to those outstanding on February 8, 2014. This was the first time since the Schedule of Federal Debt was audited for fiscal year 1997 that extraordinary actions were being used and uninvested principal related to such actions existed at fiscal year-end. Many extraordinary actions taken by Treasury during the period of May 20, 2013, through September 30, 2013, resulted in federal debt securities not being issued to certain federal government accounts. Consequently, the resulting uninvested principal as of September 30, 2013, totaling \$248 billion and related interest totaling \$801 million are not reported on the fiscal year 2013 Schedule of Federal Debt. The Overview on Federal Debt Managed by the Bureau of the Fiscal Service and note 6 to the Schedules of Federal Debt provide details on (1) the extraordinary actions taken by Treasury during these periods; (2) the uninvested principal as of September 30, 2013, and related interest; and (3) the subsequent restorations of principal and interest to the affected federal government accounts by Treasury in accordance with relevant laws.

As we have previously reported, the debt limit neither restricts Congress's ability to pass spending and revenue legislation that affects the level of federal debt nor otherwise constrains fiscal policy; it restricts Treasury's authority to borrow to finance the decisions already enacted by Congress

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<sup>8</sup>Pub. L. No. 113-46, § 1002, 127 Stat. 558, 566-67 (Oct. 17, 2013).

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and the President.<sup>9</sup> The United States benefits from the confidence investors have that debt backed by the full faith and credit of the United States will be honored. As we have also previously reported, delays in raising the debt limit can create uncertainty in the Treasury market and lead to higher Treasury borrowing costs. We estimated, as reported in July 2012, that delays in raising the debt limit in 2011 led to an increase in Treasury's borrowing costs of about \$1.3 billion in fiscal year 2011. However, this does not account for the multiyear effects on increased costs for Treasury securities that remain outstanding after fiscal year 2011. To avoid such uncertainty and related borrowing costs, in both our February 2011 and July 2012 reports related to the debt limit, we noted that Congress should consider ways to better link decisions about the debt limit with decisions about spending and revenue to avoid potential disruptions to the Treasury market and to help inform the fiscal policy debate in a timely way. As decision makers determine funding for the federal government's operations in the short term over the next few months and as they decide how to address the federal government's long-term fiscal challenges,<sup>10</sup> it will be important at the time such decisions are made that consideration be given as to the impact the decisions will have on the level of federal debt.

Federal financing needs increased in recent years, in part because of the persistent effects of the economic downturn and its impact on the federal deficit. This trend was at least in part reversed in the most recent fiscal year; the reported federal deficit for fiscal year 2013 was \$680 billion, down from the fiscal year 2012 reported federal deficit of \$1,089 billion. Debt held by the public increased slightly as a percentage of gross domestic product (GDP), from roughly 70 percent of GDP at the end of fiscal year 2012 to roughly 72 percent at the end of fiscal year 2013. Whether federal debt held by the public increases over the next several years depends in part on whether Congress and the President further amend the Balanced Budget and Emergency Deficit Control Act (BBEDCA), which provides discretionary spending limits through fiscal

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<sup>9</sup>GAO, *Debt Limit: Analysis of 2011-2012 Actions Taken and Effect of Delayed Increase on Borrowing Costs*, [GAO-12-701](#) (Washington, D.C.: July 23, 2012), and *Debt Limit: Delays Create Debt Management Challenges and Increase Uncertainty in the Treasury Market*, [GAO-11-203](#) (Washington, D.C.: Feb. 22, 2011).

<sup>10</sup>For more information, see GAO, *The Federal Government's Long-Term Fiscal Outlook: Spring 2013 Update*, [GAO-13-481SP](#) (Washington, D.C.: April 2013).

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year 2021.<sup>11</sup> Over the longer term, debt held by the public as a share of GDP is expected to grow as a result of the structural imbalance between revenue and spending driven on the spending side by rising health care costs and demographics. Increasing numbers of baby-boom generation members are becoming eligible for Social Security retirement benefits and for Medicare. In addition, although health care spending growth recently slowed, it has been growing faster than the overall economy over the past several decades and is expected to continue to grow at an increased rate as more members of the baby-boom generation retire and become eligible for federal health programs. The aging of the population and rising health care costs will continue to put upward pressure on spending and, absent action to address the growing imbalance between spending and revenue, the federal government faces an unsustainable growth in debt.

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We are sending copies of this report to interested congressional committees, the Fiscal Assistant Secretary of the Treasury, the Commissioner of the Bureau of the Fiscal Service, the Inspector General of the Department of the Treasury, the Director of the Office of Management and Budget, and other agency officials. In addition, this report is available at no charge on the GAO website at <http://www.gao.gov>.

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<sup>11</sup>The Budget Control Act of 2011 (Pub. L. No. 112-25), amending BBEDCA, imposed discretionary spending limits for fiscal years 2012 to 2021 to reduce projected spending by about \$1 trillion. The Budget Control Act also established the Joint Select Committee on Deficit Reduction, which was tasked with proposing legislation to reduce the deficit by an additional \$1.2 trillion through fiscal year 2021. The Joint Committee failed to report a proposal, and Congress and the President did not enact legislation. This failure triggered the sequestration process in BBEDCA's section 251A, which is classified, as amended, at 2 U.S.C. § 901a. Section 251A required the Office of Management and Budget to calculate, and the President to order, a sequestration of discretionary and direct spending on March 1, 2013. Section 251A also provides for an annual reduction of the discretionary spending limits and a sequestration of direct spending from fiscal years 2014 to 2021.

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If you or your staff have any questions concerning this report, please contact me at (202) 512-3406 or [engelg@gao.gov](mailto:engelg@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report.



Gary T. Engel  
Director  
Financial Management  
and Assurance



## Independent Auditor's Report

To the Commissioner of the Bureau of the Fiscal Service

In our audits of the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service (Schedule of Federal Debt)<sup>1</sup> for the fiscal years ended September 30, 2013, and 2012, we found

- the Schedules of Federal Debt for the fiscal years ended September 30, 2013, and 2012, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles;
- although internal controls could be improved, the Bureau of the Fiscal Service (Fiscal Service) maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2013; and
- no reportable noncompliance for fiscal year 2013 with provisions of applicable laws, regulations, contracts, and grant agreements we tested related to the Schedule of Federal Debt.

The following sections discuss in more detail (1) our report on the Schedules of Federal Debt and on internal control over financial reporting, which includes other information included with the Schedules of Federal Debt; (2) our report on compliance with laws, regulations, contracts, and grant agreements; and (3) agency comments.

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<sup>1</sup>For previous years, the title was the Schedule of Federal Debt Managed by the Bureau of the Public Debt (BPD). On October 7, 2012, the Secretary of the Treasury (1) established the Bureau of the Fiscal Service as a bureau within the Department of the Treasury (Treasury), (2) consolidated and redesignated BPD and the Financial Management Service as the Bureau of the Fiscal Service, and (3) transferred the duties of the BPD and Financial Management Service commissioners to the Commissioner of the Bureau of the Fiscal Service. As such, the title has changed to the Schedule of Federal Debt Managed by the Bureau of the Fiscal Service.

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## Report on the Schedules of Federal Debt and on Internal Control over Financial Reporting

In connection with fulfilling our requirement to audit the consolidated financial statements of the U.S. government, we have audited the Schedules of Federal Debt because of the significance of the federal debt to the federal government's consolidated financial statements.<sup>2</sup> The Schedules of Federal Debt present the beginning balances, increases and decreases, and ending balances for (1) Federal Debt Held by the Public and Intragovernmental Debt Holdings, (2) the related Accrued Interest Payables, and (3) the related Net Unamortized Premiums and Discounts managed by the Department of the Treasury's (Treasury) Fiscal Service, and include accompanying notes.<sup>3</sup> We also have audited Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2013, based on criteria established under 31 U.S.C. § 3512(c), (d), commonly known as the Federal Managers' Financial Integrity Act (FMFIA).

We conducted our audits in accordance with U.S. generally accepted government auditing standards. We believe that the audit evidence we obtained is sufficient and appropriate to provide a basis for our audit opinions.

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## Management's Responsibility

Fiscal Service management is responsible for (1) the preparation and fair presentation of the Schedules of Federal Debt in accordance with U.S. generally accepted accounting principles; (2) preparing and presenting other information included in documents containing the audited Schedules of Federal Debt and auditor's report, and ensuring the consistency of that information with the audited Schedules of Federal Debt; (3) maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of Schedules of Federal Debt that are free from material misstatement, whether due to fraud or

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<sup>2</sup>31 U.S.C. § 331(e)(2). Because Fiscal Service is a bureau within the Treasury, federal debt and related activity and balances managed by it are also significant to the consolidated financial statements of the Department of the Treasury (see 31 U.S.C. § 3515(b)).

<sup>3</sup>Debt held by the public represents federal debt issued by Treasury and held by investors outside of the federal government, including individuals, corporations, state or local governments, the Federal Reserve, and foreign governments. Intragovernmental debt holdings represent federal debt owed by Treasury to federal government accounts, primarily federal trust funds such as Social Security and Medicare.

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error; (4) evaluating the effectiveness of internal control over financial reporting based on the criteria established under FMFIA; and (5) providing its assertion about the effectiveness of internal control over financial reporting as of September 30, 2013, based on its evaluation, included in the accompanying Management's Report on Internal Control over Financial Reporting in appendix I.

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## Auditor's Responsibility

Our responsibility is to express an opinion on the Schedules of Federal Debt and an opinion on Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt based on our audits. U.S. generally accepted government auditing standards require that we plan and perform the audits to obtain reasonable assurance about whether the Schedules of Federal Debt are free from material misstatement, and whether effective internal control over financial reporting was maintained in all material respects. We are also responsible for applying certain limited procedures to the other information included with the Schedules of Federal Debt.

An audit of the Schedules of Federal Debt involves performing procedures to obtain audit evidence about the amounts and disclosures in the Schedules of Federal Debt. The procedures selected depend on the auditor's judgment, including the auditor's assessment of the risks of material misstatement of the Schedules of Federal Debt, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the Schedules of Federal Debt in order to design audit procedures that are appropriate in the circumstances. An audit of the Schedules of Federal Debt also involves evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the Schedules of Federal Debt. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, evaluating the design and operating effectiveness of internal control over financial reporting based on the assessed risk, and testing relevant internal control over financial reporting. Our audit of internal control also considered Fiscal Service's process for evaluating and reporting on internal control over financial reporting relevant to the Schedule of Federal Debt based on criteria established under FMFIA. Our audits also included performing such other procedures as we considered necessary in the circumstances.

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We did not evaluate all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing performance information and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting. Our internal control testing was for the purpose of expressing an opinion on whether effective internal control over financial reporting relevant to the Schedule of Federal Debt was maintained, in all material respects. Consequently, our audit may not identify all deficiencies in internal control over financial reporting relevant to the Schedule of Federal Debt that are less severe than a material weakness.<sup>4</sup>

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## Definitions and Inherent Limitations of Internal Control over Financial Reporting

Internal control over financial reporting relevant to the Schedule of Federal Debt is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of the Schedule of Federal Debt in accordance with U.S. generally accepted accounting principles, and (2) transactions related to the Schedule of Federal Debt are executed in accordance with laws governing the use of budget authority and with other applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on the Schedule of Federal Debt.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements due to fraud or error. We also caution that projecting any evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

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<sup>4</sup>A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

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**Opinion on the Schedules of Federal Debt**

In our opinion, the Schedules of Federal Debt present fairly, in all material respects, Federal Debt Managed by Fiscal Service and the related Accrued Interest Payables and Net Unamortized Premiums and Discounts as of September 30, 2013, and 2012, and the related increases and decreases for the fiscal years then ended in accordance with U.S. generally accepted accounting principles.

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**Opinion on Internal Control over Financial Reporting**

In our opinion, although internal controls could be improved, Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2013, based on criteria established under FMFIA.

We identified a significant deficiency in Fiscal Service's internal control over financial reporting, which although not a material weakness, is important enough to merit the attention of those charged with governance of Fiscal Service.<sup>5</sup> This deficiency, described in more detail below, concerns Fiscal Service's information systems controls.

We will be reporting additional details concerning this significant deficiency separately to Fiscal Service management, along with recommendations for corrective actions. We also identified other deficiencies in Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt that we do not consider to be material weaknesses or significant deficiencies. Nonetheless, these deficiencies warrant Fiscal Service management's attention. We have communicated these matters to Fiscal Service management and, where appropriate, will report on them separately.

**Significant Deficiency in Internal Control Related to Information Systems**

During fiscal year 2013, we identified new deficiencies in information systems controls that along with unresolved control deficiencies from prior audits, collectively represent a significant deficiency in Fiscal Service's internal control over financial reporting. Specifically, the deficiencies related to general information systems controls in the areas of security

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<sup>5</sup>A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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management, access controls, and configuration management.<sup>6</sup> For most of these deficiencies, Fiscal Service either had not developed and implemented adequate policies and procedures or was not consistently following its policies and procedures. Further, several of these information systems control deficiencies had not been detected by Fiscal Service, and certain previously reported control deficiencies that Fiscal Service informed us it had addressed continued to be present. The potential effect of these deficiencies on the Schedule of Federal Debt financial reporting was mitigated primarily by Fiscal Service's physical security measures and compensating management and reconciliation controls designed to detect potential misstatements on the Schedule of Federal Debt. Nevertheless, these deficiencies, collectively, significantly increase the risk of unauthorized access, loss, modification, or disclosure of sensitive data and programs and disruption of critical operations, and therefore merit the attention of those charged with governance of Fiscal Service.

Fiscal Service relies on a number of information systems to manage the federal debt. In late fiscal year 2011, Treasury began consolidating the data centers and related operations of Treasury's Bureau of the Public Debt and Financial Management Service. In addition, in fiscal year 2013, Fiscal Service began testing a new general ledger system and is implementing the new system in fiscal year 2014. Further, certain systems that process federal debt are moving to a more distributed computing environment, which presents different risks.<sup>7</sup> These continuing changes can introduce risks that require corresponding changes to controls, can hinder the effective operation of controls, and may have contributed to some of the control deficiencies comprising the significant deficiency. Also, such changes could hamper Fiscal Service's ability to effectively and timely resolve the identified control deficiencies and could result in additional control deficiencies. Consequently, addressing the significant deficiency in this environment will require increased focus on

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<sup>6</sup>Security management provides a framework and continuing cycle of activity for managing risk, developing security policies, assigning responsibilities, and monitoring the adequacy of the entity's computer-related controls. Access controls limit or detect access to computer resources such as data, programs, equipment, and facilities, thereby protecting them against unauthorized modification, loss, and disclosure. Configuration management prevents unauthorized changes to information system resources, such as software programs and hardware configurations, and provides reasonable assurance that systems are configured and operating securely and as intended.

<sup>7</sup>Distributed environments enable multiple computer processing units to communicate with each other.

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assessing risks associated with these changes, monitoring the effectiveness of the operation of controls, and designing and implementing effective internal controls.

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## Other Matter

### Other Information

Fiscal Service's other information, which consists of the Overview on the Schedule of Federal Debt Managed by the Bureau of the Fiscal Service, contains a wide range of information, some of which is not directly related to the Schedules of Federal Debt. This information is presented for purposes of additional analysis and is not a required part of the Schedules of Federal Debt. We read the other information included with the Schedules of Federal Debt in order to identify material inconsistencies, if any, with the audited Schedules of Federal Debt. Our audit was conducted for the purpose of forming an opinion on the Schedules of Federal Debt. We did not audit and do not express an opinion or provide any assurance on the other information.

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## Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

In connection with our audits of the Schedules of Federal Debt, we tested compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements consistent with our auditor's responsibility discussed below. We caution that noncompliance may occur and not be detected by these tests. We performed our tests of compliance in accordance with U.S. generally accepted government auditing standards.

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### Management's Responsibility

Fiscal Service management is responsible for complying with laws, regulations, contracts, and grant agreements applicable to Fiscal Service.

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### Auditor's Responsibility

Our responsibility is to test compliance with selected provisions of laws, regulations, contracts, and grant agreements applicable to Fiscal Service that have a direct effect on the determination of material amounts and disclosures in the Schedules of Federal Debt, and perform certain other limited procedures. Accordingly, we did not test compliance with all laws, regulations, contracts, and grant agreements applicable to Fiscal Service.

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## Results of Our Tests for Compliance with Laws, Regulations, Contracts, and Grant Agreements

Our tests for compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements disclosed no instances of noncompliance for fiscal year 2013 that would be reportable under U.S. generally accepted government auditing standards. However, the objective of our tests was not to provide an opinion on compliance with laws, regulations, contracts, and grant agreements applicable to Fiscal Service. Accordingly, we do not express such an opinion.

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## Intended Purpose of Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

The purpose of this report is solely to describe the scope of our testing of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements, and the results of that testing, and not to provide an opinion on compliance. This report is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering compliance. Accordingly, this report on compliance with laws, regulations, contracts, and grant agreements is not suitable for any other purpose.

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## Agency Comments

In commenting on a draft of this report, Fiscal Service's Commissioner concurred with our conclusions. Fiscal Service's comments are reprinted in their entirety in appendix II.



Gary T. Engel  
Director  
Financial Management and Assurance

December 4, 2013

# Overview, Schedules, and Notes

## Overview on Federal Debt Managed by the Bureau of the Fiscal Service

### Overview on Federal Debt Managed by the Bureau of the Fiscal Service

#### Gross Federal Debt Outstanding

Federal debt managed by the Bureau of the Fiscal Service (Fiscal Service) comprises debt held by the public and debt held by certain federal government accounts (under 31 U.S.C. § 3101), the latter of which is referred to as intragovernmental debt holdings. As of September 30, 2013 and September 30, 2012, outstanding gross federal debt managed by Fiscal Service totaled \$16,732 billion and \$16,059 billion, respectively.<sup>1</sup> As Figure 1 illustrates, intragovernmental debt holdings and debt held by the public increased by \$443 billion and \$3,718 billion, respectively, from September 30, 2009 to September 30, 2012. The primary reason for the increases in intragovernmental debt holdings is the excess annual receipts (including interest earnings) over disbursements in the Federal Old-Age and Survivors Insurance Trust Fund, Civil Service Retirement and Disability Fund (CSRDF), Military Retirement Fund, and DOD Medicare-Eligible Retiree Health Care Fund. From September 30, 2012 to September 30, 2013, intragovernmental debt holdings decreased by \$33 billion while debt held by the public increased by \$706 billion. Because of a delay in raising the debt limit, the Department of Treasury (Treasury) had to take extraordinary actions to meet the government's obligations as they came due without exceeding the debt limit, which included suspension of investments to the CSRDF and Postal Service Retiree Health Benefits Fund (Postal Benefits Fund). As of September 30, 2013, the delay still existed and suspension of investments for these funds continued, which contributed to the decrease in the intragovernmental debt holdings. The increases in debt held by the public are due primarily to total federal spending exceeding total federal revenues. As of September 30, 2013, gross debt held by the public totaled \$11,976 billion and gross intragovernmental debt holdings totaled \$4,756 billion. Gross federal debt (with some adjustments) is subject to a statutory debt limit. As of September 30, 2013 and September 30, 2012, the statutory debt limit was \$16,699 billion and \$16,394 billion, respectively, and debt subject to the statutory debt limit was \$16,699 billion and \$16,027 billion, respectively.

**Figure 1 Total Gross Federal Debt Outstanding (in billions)**



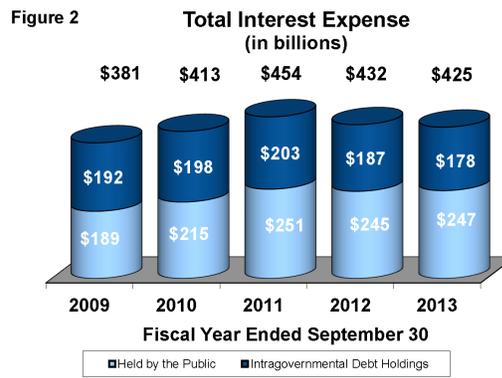
<sup>1</sup> Federal debt outstanding reported here differs from the amount reported in the Financial Report of the United States Government because of the securities not maintained or reported by Fiscal Service which are issued by the Federal Financing Bank and other specific securities issued outside of the authority of Title 31, U.S. Code, section 3101.

### ***Interest Expense***

Interest expense incurred during fiscal year 2013 consists of (1) interest accrued and paid on debt held by the public or credited to accounts holding intragovernmental debt during the fiscal year, (2) interest accrued during the fiscal year, but not yet paid on debt held by the public or credited to accounts holding intragovernmental debt, and (3) net amortization of premiums and discounts. The primary components of interest expense are interest paid on the debt held by the public and interest credited to federal government trust funds and other federal government accounts that hold Treasury securities. The interest paid on the debt held by the public affects the current spending of the federal government and represents the burden of servicing its debt (i.e., payments to outside creditors). Interest credited to federal government trust funds and other federal government accounts, on the other hand, does not result in an immediate outlay of the Federal Government because one part of the government pays the interest and another part receives it. However, this interest represents a claim on future budgetary resources and hence an obligation on future taxpayers. This interest, when reinvested by the trust funds and other federal government accounts, is included in the programs' excess funds not currently needed in operations, which are invested in federal securities. For fiscal year 2013, interest expense incurred totaled \$425 billion; this consisted of interest expense on debt held by the public of \$247 billion, and \$178 billion in interest incurred for intragovernmental debt holdings.

As Figure 2 illustrates, interest expense increased from fiscal year 2009 through 2011 due primarily to an increase in Treasury notes and bonds outstanding, which had higher average interest rates than Treasury bills. Interest expense decreased for fiscal year 2012 due primarily to a decrease in the average interest rates for Treasury notes, bonds and Treasury Inflation-Protected Securities (TIPS). From fiscal year 2012 to 2013, total interest expense decreased from \$432 billion to \$425 billion. This decrease results from an increase of \$2 billion in interest expense on debt held by the public offset by a \$9 billion decrease in interest expense on intragovernmental debt holdings. The \$2 billion increase in interest expense on debt held by the public results from the overall increase in the outstanding debt held by the public being almost fully offset by a decrease in the average interest rates for Treasury notes, bonds, and TIPS. Average interest rates on federal debt held by the public, marketable have continued to decrease while the average interest rate on federal debt held by the public, nonmarketable increased this fiscal year. The suspension of investments to the Government Securities Investment Fund of the Federal Employees' Retirement System (G-Fund) and the suspension of new issuances of State and Local Government Series (SLGS) securities related to the extraordinary actions taken due to the aforementioned delay in raising the debt limit resulted in a decrease in nonmarketable debt of \$141 billion from that of fiscal year 2012. Since these suspended investments had lower interest rates than the average, the result is an overall increase in the nonmarketable average interest rate. The \$9 billion decrease in interest expense on intragovernmental debt holdings results primarily from the decrease in the average interest rates on intragovernmental debt holdings. Average interest rates on principal balances outstanding as of September 30, 2013 and 2012, are disclosed in the Notes to the Schedules of Federal Debt.

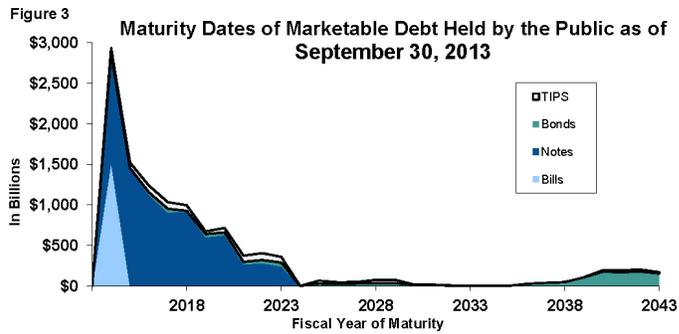
*Interest Expense, cont.*



**Debt Held by the Public**

Debt held by the public primarily represents the amount the Federal Government has borrowed to finance cumulative cash deficits. During fiscal year 2013, Treasury primarily used the existing suite of securities to meet the borrowing needs of the Federal Government while increasing its offerings of longer term securities to extend the average length of maturity. As a result, Treasury bills decreased by \$85 billion; whereas, Treasury notes, bonds, and TIPS increased by \$635 billion, \$168 billion, and \$129 billion, respectively, in fiscal year 2013. As of September 30, 2013 and 2012, gross debt held by the public totaled \$11,976 billion and \$11,270 billion, respectively (see Figure 1), an increase of \$706 billion. This increase was primarily the result of borrowings needed to finance the government's fiscal year 2013 deficit. Due to an increase in short term debt issuances, as compared to the prior year, the total dollar amount of activity for both borrowings and repayments of debt held by the public increased for fiscal year 2013.

As of September 30, 2013, \$11,577 billion, or 97 percent, of the securities that constitute debt held by the public were marketable, meaning that once the Federal Government issues them, they can be resold by whoever owns them. Marketable debt is made up of Treasury bills, Treasury notes, Treasury bonds, and TIPS with maturity dates ranging from less than 1 year out to 30 years. Of the marketable securities currently held by the public as of September 30, 2013, \$6,729 billion, or 58 percent, will mature within the next 4 years (see Figure 3). As of September 30, 2013 and 2012, notes and TIPS held by the public maturing within the next 10 years totaled \$8,436 billion and \$7,646 billion, respectively, an increase of \$790 billion.



***Debt Held by the Public, cont.***

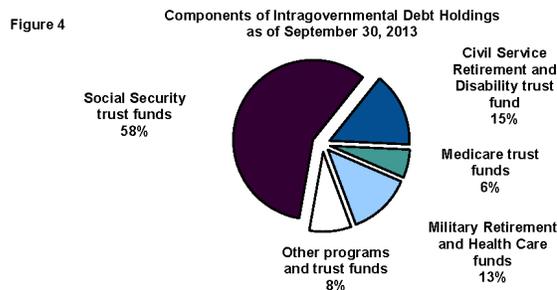
The Federal Government also issues to the public nonmarketable securities, which cannot be resold, and have maturity dates ranging from on demand out to 40 years. As of September 30, 2013, nonmarketable securities totaled \$399 billion, or 3 percent of debt held by the public. As of that date, nonmarketable securities primarily consisted of savings securities totaling \$180 billion, SLGS securities totaling \$124 billion, and Government Account Series securities totaling \$60 billion. From fiscal year end 2012 to 2013, total nonmarketable securities decreased from \$539 billion to \$399 billion. This decrease results from the suspension of investments to the G-Fund and the suspension of new issuances of SLGS securities related to the extraordinary actions taken due to the delay in raising the debt limit that continued to exist as of September 30, 2013.

The Federal Reserve Banks (FRBs) act as fiscal agents for Treasury, as permitted by the Federal Reserve Act. As fiscal agents for Treasury, the FRBs play a significant role in the processing of marketable book-entry securities and paper U.S. savings bonds. For marketable book-entry securities, selected FRBs receive bids, issue book-entry securities to awarded bidders, and collect payments on behalf of Treasury; and make interest and redemption payments from Treasury's account to the accounts of security holders. For paper U.S. savings bonds, selected FRBs print and deliver savings bonds purchased with federal income tax refunds; and redeem savings bonds, including handling the related transfers of cash.

**Intragovernmental Debt Holdings**

Intragovernmental debt holdings represent balances of Treasury securities held by over 230 individual federal government accounts with either the authority or the requirement to invest excess receipts in special U.S. Treasury securities that are guaranteed for principal and interest by the full faith and credit of the U.S. Government. Intragovernmental debt holdings primarily consist of balances in the Social Security, Medicare, Military Retirement and Health Care, and Civil Service Retirement and Disability trust funds.<sup>2</sup> As of September 30, 2013, such funds accounted for \$4,354 billion, or 92 percent, of the \$4,756 billion intragovernmental debt holdings balances (see Figure 4). As of September 30, 2013 and 2012, gross intragovernmental debt holdings totaled \$4,756 billion and \$4,789 billion, respectively (see Figure 1), a decrease of \$33 billion.

The majority of intragovernmental debt holdings are Government Account Series (GAS) securities. GAS securities consist of par value securities and market-based securities, with terms ranging from on demand out to 30 years. Par value securities are issued and redeemed at par (100 percent of the face value), regardless of current market conditions. Market-based securities, however, can be issued at a premium or discount and are redeemed at par value on the maturity date or at market value if redeemed before the maturity date.



<sup>2</sup> The Social Security trust funds consist of the Federal Old-Age and Survivors Insurance Trust Fund and the Federal Disability Insurance Trust Fund. The Medicare trust funds are made up of the Federal Hospital Insurance Trust Fund and the Federal Supplementary Medical Insurance Trust Fund. The Military Retirement and Health Care Funds consist of the Military Retirement Fund and the DOD Medicare-Eligible Retiree Health Care Fund.

### ***Significant Events in Fiscal Year 2013***

#### **FY 2013 Establishment of the Bureau of the Fiscal Service**

On October 7, 2012, the Secretary of the Treasury (1) established the Bureau of the Fiscal Service as a bureau within the Department of the Treasury, (2) consolidated and redesignated the Bureau of the Public Debt and the Financial Management Service as the Bureau of the Fiscal Service, and (3) transferred the duties of the Bureau of the Public Debt and Financial Management Service commissioners to the Commissioner of the Bureau of the Fiscal Service. Beyond the financial and operational benefits, this consolidation will enable the Department of the Treasury to better address the financial management needs of the federal government and realize administrative efficiencies while retaining existing core federal financial management responsibilities.

#### **Statutory Debt Limit Raised**

Prior to the enactment of the “No Budget, No Pay Act of 2013” (Public Law No 113-3), which was signed into law on February 4, 2013, delays in raising the statutory debt limit occurred that required Treasury to depart from its normal debt management procedures and invoke legal authorities to avoid exceeding the statutory debt limit. On December 31, 2012, the Secretary of the Treasury declared a debt issuance suspension period beginning on that date. During the period of December 31, 2012 through February 3, 2013, extraordinary actions taken by Treasury included (1) suspending investments to the G-Fund, CSRDF, Postal Benefits Fund, and Exchange Stabilization Fund (ESF) and (2) redeeming certain investments held by CSRDF earlier than normal. Treasury also suspended new issuances of SLGS securities.

On February 4, 2013, a temporary suspension of the statutory debt limit through May 18, 2013 was enacted. In accordance with relevant laws, on February 4, 2013, Fiscal Service restored uninvested principal to the G-Fund and CSRDF totaling \$31 billion. Also, in accordance with relevant laws, Fiscal Service restored the interest related to the suspended investments and early redemptions to the G-Fund, CSRDF, and Postal Benefits Fund totaling \$20 million by June 28, 2013. Postal Benefits Fund and ESF were fully invested prior to February 4, 2013, and ESF is not entitled to foregone interest. At the end of the temporary suspension of the statutory debt limit, consistent with Public Law No. 113-3, the debt limit was raised on May 19, 2013, to \$16,699 billion, which was the amount of qualifying federal debt securities outstanding on that date.

***Significant Events in Fiscal Year 2013, cont.***

**Additional Debt Issuance Suspension Period**

Beginning May 20, 2013, Treasury faced an additional debt issuance suspension period. During the remainder of fiscal year 2013, Treasury departed from its normal debt management procedures and invoked legal authorities to avoid exceeding the debt limit. During this period, extraordinary actions taken by Treasury included (1) suspending investments to the G-Fund, CSRDF, and Postal Benefits Fund and (2) redeeming certain investments held by CSRDF earlier than normal. Additionally, Treasury suspended new issuances of SLGS securities and issued cash management bills to manage short-term financing needs.

On September 30, 2013, a delay in raising the statutory debt limit still existed with Treasury continuing to use extraordinary actions to meet the government's obligations as they come due without exceeding the debt limit. Many extraordinary actions taken by Treasury during the period of May 20, 2013 through September 30, 2013, resulted in federal debt securities not being issued to certain federal government accounts. Consequently, the resulting uninvested principal as of September 30, 2013, totaling \$247,827 million and related interest totaling \$801 million are not reported on the Schedule of Federal Debt. Such uninvested principal and related interest are disclosed in Note 6 to the Schedule of Federal Debt.

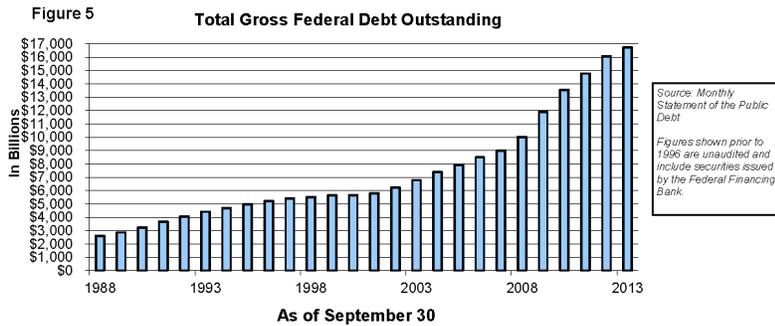
**Floating Rate Notes**

In August 2012, Treasury announced that it plans to develop a floating rate note program to complement the existing suite of securities issued and to help achieve the objective of financing the government at the lowest cost over time. Treasury published amendments to its marketable securities auction rules to accommodate the auction and issuance of floating rate notes on July 31, 2013. Treasury's introduction of the floating rate note will provide a number of benefits, including assisting Treasury in managing the maturity profile of the nation's marketable debt outstanding, expanding Treasury's investor base, and helping to finance the government at the lowest cost over time.

The floating rate note is a security that has an interest payment that can change over time. Treasury floating rate notes will be indexed to the highest accepted discount rate (high rate) of the most recent 13-week Treasury bill auction. The bidding process, the minimum and maximum purchase and award amounts, and the award methodology are the same as for other marketable securities. Treasury will announce specific terms and conditions of each issue, such as the auction date, issue date, and the public offering amount, prior to each auction. The first floating rate note auction is expected to occur in January 2014.

### Historical Perspective

Federal debt outstanding is one of the largest legally binding obligations of the Federal Government. Nearly all the federal debt has been issued by the Treasury with a small portion being issued by other federal government agencies. Treasury issues debt securities for two principal reasons, (1) to borrow needed funds to finance the current operations of the Federal Government and (2) to provide an investment and accounting mechanism for certain federal government accounts' (primarily federal trust funds) excess receipts. Total gross federal debt outstanding has dramatically increased over the past 25 years from \$2,602 billion as of September 30, 1988, to \$16,732 billion as of September 30, 2013 (see Figure 5). Large budget deficits emerged during the 1980's due to tax policy decisions and increased outlays for defense and domestic programs. Through fiscal year 1997, annual federal deficits continued to be large and debt continued to grow at a rapid pace. As a result, total federal debt doubled between 1988 and 1997.

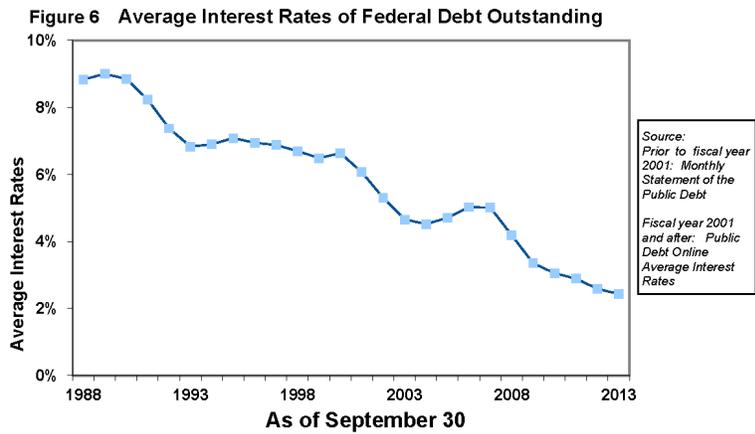


By fiscal year 1998, federal debt held by the public was beginning to decline. In fiscal years 1998 through 2001, the amount of debt held by the public fell by \$476 billion, from \$3,815 billion to \$3,339 billion. However, federal debt held by the public began to increase in fiscal year 2002, primarily as a result of higher federal outlays. Federal debt held by the public increased by 51.2 percent from fiscal year 2002 through fiscal year 2007. From fiscal year 2008 through fiscal year 2013, federal debt held by the public more than doubled, rising by \$6,927 billion. This increase was primarily a result of the economic downturn and the federal government's response to it. Since fiscal year 2002, debt held by the public has increased from \$3,339 billion as of September 30, 2001 to \$11,976 billion as of September 30, 2013.

**Historical Perspective, cont.**

Even in those years where debt held by the public declined, total federal debt increased because of increases in intragovernmental debt holdings. Over the past 4 fiscal years, intragovernmental debt holdings increased by \$410 billion, from \$4,346 billion as of September 30, 2009, to \$4,756 billion as of September 30, 2013. The increase in intragovernmental debt holdings would have been greater had there not been a suspension of investments for certain federal government accounts related to extraordinary actions taken due to the delay in raising the debt limit in effect at September 30, 2013. By law, federal government accounts, including trust funds, have the authority or are required to invest their excess annual receipts (including interest earnings) over disbursements in federal securities. As a result, the intragovernmental debt holdings balances primarily represent the cumulative surplus of funds due to the trust funds' cumulative annual excess of tax receipts, interest credited, and other collections compared to spending.

As shown in Figure 6, interest rates have fluctuated over the past 25 years. The average interest rates reflected here represent the original issue weighted effective yield on debt held by the public and intragovernmental debt holdings outstanding at the end of the fiscal year.



**Significant Change After Fiscal Year 2013 Affecting Federal Debt**

A delay in raising the statutory debt limit existed at the end of fiscal year 2013 and lasted until October 17, 2013, when the Continuing Appropriations Act, 2014, (Public Law No 113-46) was enacted. During the period of October 1 through October 16, 2013, Treasury continued to use extraordinary actions to meet the government's obligations as they came due without exceeding the debt limit. In addition to continuing with the actions used from May 20, 2013 through September 30, 2013, Treasury (1) exchanged \$9 billion of Treasury securities held by the CSRDF for securities issued by the Federal Financing Bank and (2) began suspending investments to the ESF. On October 17, 2013, a temporary suspension of the statutory debt limit through February 7, 2014 was enacted. The amounts related to the restoration of uninvested principal as of October 16, 2013, and related interest for the period May 20, 2013 through October 16, 2013, are disclosed in Note 6 to the Schedules of Federal Debt. The Continuing Appropriations Act, 2014, established a process that may result in an increase of the statutory debt limit on February 8, 2014. This increase will be determined by the change in qualifying federal debt securities outstanding on October 17, 2013 compared to those outstanding on February 8, 2014.

Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

Schedules of Federal Debt

Managed by the Bureau of the Fiscal Service  
For the Fiscal Years Ended September 30, 2013 and 2012  
(Dollars in Millions)

	Federal Debt					
	Held by the Public			Intragovernmental Debt Holdings		
	Principal (Note 2)	Accrued Interest Payable	Net Unamortized Premiums/ (Discounts)	Principal (Note 3)	Accrued Interest Payable	Net Unamortized Premiums/ (Discounts)
<i>Balance as of September 30, 2011</i>	<b>\$10,127,031</b>	<b>\$51,470</b>	<b>(\$29,538)</b>	<b>\$4,654,374</b>	<b>\$47,778</b>	<b>\$47,624</b>
<b>Increases</b>						
Borrowings from the Public	7,761,885		4,995			
Net Increase in Intragovernmental Debt Holdings				134,677		13,242
Accrued Interest (Note 4)		240,097			191,656	
<b>Total Increases</b>	<b>7,761,885</b>	<b>240,097</b>	<b>4,995</b>	<b>134,677</b>	<b>191,656</b>	<b>13,242</b>
<b>Decreases</b>						
Repayments of Debt Held by the Public	6,619,330					
Interest Paid		234,345			193,886	
Net Amortization (Note 4)			(5,318)			4,616
<b>Total Decreases</b>	<b>6,619,330</b>	<b>234,345</b>	<b>(5,318)</b>	<b>0</b>	<b>193,886</b>	<b>4,616</b>
<i>Balance as of September 30, 2012</i>	<b>11,269,586</b>	<b>57,222</b>	<b>(19,225)</b>	<b>4,789,051</b>	<b>45,548</b>	<b>56,250</b>
<b>Increases</b>						
Borrowings from the Public	8,155,584		(10,112)			
Net Increase in Intragovernmental Debt Holdings - Premiums						21,004
Accrued Interest (Note 4)		242,689			185,437	
<b>Total Increases</b>	<b>8,155,584</b>	<b>242,689</b>	<b>(10,112)</b>	<b>0</b>	<b>185,437</b>	<b>21,004</b>
<b>Decreases</b>						
Repayments of Debt Held by the Public	7,448,891					
Net Decrease in Intragovernmental Debt Holdings - Principal				33,336		
Interest Paid		248,716			187,856	
Net Amortization (Note 4)			(4,893)			7,807
<b>Total Decreases</b>	<b>7,448,891</b>	<b>248,716</b>	<b>(4,893)</b>	<b>33,336</b>	<b>187,856</b>	<b>7,807</b>
<i>Balance as of September 30, 2013</i>	<b>\$11,976,279</b>	<b>\$51,195</b>	<b>(\$24,444)</b>	<b>\$4,755,715</b>	<b>\$43,129</b>	<b>\$69,447</b>

The accompanying notes are an integral part of these schedules.

## Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

*Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service  
For the Fiscal Years Ended September 30, 2013 and 2012*

*(Dollars in Millions)*

### **Note 1. Significant Accounting Policies**

#### Basis of Presentation

The Schedules of Federal Debt Managed by the Bureau of the Fiscal Service (Fiscal Service) have been prepared to report fiscal year 2013 and fiscal year 2012 balances and activity relating to monies borrowed from the public and certain federal government accounts under 31 U.S.C. § 3101 to fund the operations of the U.S. government. Permanent, indefinite appropriations are available for the payment of interest on the federal debt and the redemption of Treasury securities.

#### Reporting Entity

The Constitution empowers the Congress to borrow money on the credit of the United States. The Congress has authorized the Secretary of the Treasury to borrow monies to operate the federal government within a statutory debt limit. Title 31, U.S. Code authorizes Treasury to prescribe the debt instruments and otherwise limit and restrict the amount and composition of the debt. Fiscal Service, an organizational entity within the Department of the Treasury, is responsible for issuing Treasury securities in accordance with such authority and to account for the resulting debt. In addition, Fiscal Service maintains an investment program for federal government accounts, including trust funds, that have legislative authority to invest temporary cash reserves not needed for current benefits and expenses. Fiscal Service issues and redeems Treasury securities for these federal government accounts based on data provided by the respective program agencies and other Treasury entities. Fiscal Service also issues other specific securities outside of the authority of 31 U.S.C. § 3101, such as HOPE Bonds, that are not reported on the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service.

#### Basis of Accounting

The schedules were prepared in accordance with U.S. generally accepted accounting principles and from Fiscal Service's automated debt accounting system. Accounting principles generally accepted for Federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB), which is the official body for setting accounting standards of the Federal government. The FASAB issued the Statement of Federal Financial Accounting Standards (SFFAS) No. 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board* in July 2009. SFFAS No. 34 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of general purpose financial reports of federal reporting entities that are presented in accordance with Federal generally accepted accounting principles.

Interest costs are recorded as expenses when incurred, instead of when paid. Certain Treasury securities are issued at a discount or premium. These discounts and premiums are amortized over the term of the security using an interest method for all long term securities and the straight line method for short term securities. The Department of the Treasury also issues Treasury Inflation-Protected Securities (TIPS). The principal for TIPS is adjusted daily over the life of the security based on the Consumer Price Index for all Urban Consumers.

*Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service  
For the Fiscal Years Ended September 30, 2013 and 2012*

*(Dollars in Millions)*

**Note 2. Federal Debt Held by the Public**

As of September 30, 2013 and 2012, Federal Debt Held by the Public consisted of the following:

	2013		2012	
	Amount	Average Interest Rates	Amount	Average Interest Rates
Marketable:				
Treasury Bills	\$ 1,527,909	0.1 %	\$1,613,026	0.1%
Treasury Notes	7,750,336	1.8 %	7,114,960	2.0%
Treasury Bonds	1,363,114	5.1 %	1,194,715	5.4%
TIPS	936,041	1.1 %	807,469	1.4%
Total Marketable	<u>\$ 11,577,400</u>		<u>\$10,730,170</u>	
Nonmarketable	<u>\$ 398,879</u>	2.4 %	<u>\$539,416</u>	2.1%
Total Federal Debt Held by the Public	<u>\$ 11,976,279</u>		<u>\$11,269,586</u>	

Treasury issues marketable bills usually at a discount, but may also issue at par, and pays the par amount of the security upon maturity. The average interest rate on Treasury bills represents the original issue effective yield on securities outstanding as of September 30, 2013 and 2012. Treasury bills are issued with a term of one year or less.

Treasury issues marketable notes and bonds as long-term securities that pay semi-annual interest based on the securities' stated interest rate. These securities are issued at either par value or at an amount that reflects a discount or a premium. The average interest rate on marketable notes and bonds represents the stated interest rate adjusted by any discount or premium on securities outstanding as of September 30, 2013 and 2012. Treasury notes are issued with a term of 2 – 10 years and Treasury bonds are issued with a term of more than 10 years.

Treasury also issues TIPS that have interest and redemption payments that are tied to the Consumer Price Index for all Urban Consumers, a widely used measure of inflation. TIPS are issued with a term of 5 years or more. At maturity, TIPS are redeemed at the inflation-adjusted principal amount, or the original par value, whichever is greater. TIPS pay a semi-annual fixed rate of interest applied to the inflation-adjusted principal. The average interest rate on TIPS represents the stated interest rate on principal plus inflation, adjusted by any discount or premium on securities outstanding as of September 30, 2013 and 2012. The TIPS Federal Debt Held by the Public inflation-adjusted principal balance includes inflation of \$88,524 million and \$77,909 million as of September 30, 2013 and 2012, respectively.

*Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service  
For the Fiscal Years Ended September 30, 2013 and 2012*

*(Dollars in Millions)*

**Note 2. Federal Debt Held by the Public (continued)**

Federal Debt Held by the Public includes federal debt held outside of the U. S. government by individuals, corporations, Federal Reserve Banks (FRB), state and local governments, and foreign governments and central banks. As of September 30, 2013, the FRB had total holdings of \$1,930,247 million, which (1) excludes \$145,184 million in Treasury securities used in overnight reverse repurchase transactions and (2) includes a net of \$3,148 million in Treasury securities held by the FRB as collateral for securities lending activities. As of September 30, 2012, the FRB had total holdings of \$1,646,809 million, including a net of \$1,523 million in Treasury securities held by the FRB as collateral for securities lending activities. Treasury securities are held by the FRB in the FRB System Open Market Account (SOMA) for the purpose of conducting monetary policy.

Treasury issues nonmarketable securities at either par value or at an amount that reflects a discount or a premium. The average interest rate on the nonmarketable securities represents the original issue weighted effective yield on securities outstanding as of September 30, 2013 and 2012. Nonmarketable securities are issued with a term of on demand out to 40 years.

As of September 30, 2013 and 2012, nonmarketable securities consisted of the following:

	2013	2012
Domestic Series	\$ 29,995	\$29,995
Foreign Series	2,986	2,986
State and Local Government Series	124,079	158,514
United States Savings Securities	180,022	183,661
Government Account Series	60,445	162,880
Other	1,352	1,380
<b>Total Nonmarketable</b>	<b>\$ 398,879</b>	<b>\$539,416</b>

Government Account Series (GAS) securities are nonmarketable securities issued to federal government accounts. Federal Debt Held by the Public includes GAS securities issued to certain federal government accounts. One example is the GAS securities held by the Government Securities Investment Fund (G-Fund) of the federal employees' Thrift Savings Plan. Federal employees and retirees who have individual accounts own the GAS securities held by the fund. For this reason, these securities are considered part of the Federal Debt Held by the Public rather than Intragovernmental Debt Holdings. The GAS securities held by the G-Fund consist of overnight investments redeemed one business day after their issue. The net decrease in the fund's principal balance during fiscal year 2013 is included in the Repayments of Debt Held by the Public amount reported on the Schedules of Federal Debt. The net increase in the fund's principal balance during fiscal year 2012 is included in the Borrowings from the Public amount reported on the Schedules of Federal Debt.

Fiscal year-end September 30, 2012, occurred on a Sunday. As a result, \$53,003 million of marketable Treasury notes, \$35 million of Government Account Series securities, and \$1 million of State and Local Government Series securities matured but not repaid are included in the balance of the total debt held by the public as of September 30, 2012. Settlement of this debt repayment occurred on Monday, October 1, 2012.

*Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service  
For the Fiscal Years Ended September 30, 2013 and 2012*

*(Dollars in Millions)*

**Note 3. Intragovernmental Debt Holdings**

As of September 30, 2013 and 2012, Intragovernmental Debt Holdings are owed to the following:

	<u>2013</u>	<u>2012</u>
SSA: Federal Old-Age and Survivors Insurance Trust Fund	\$2,655,599	\$2,586,697
OPM: Civil Service Retirement and Disability Fund	713,761	819,444
DOD: Military Retirement Fund	421,327	376,439
HHS: Federal Hospital Insurance Trust Fund	206,010	228,292
DOD: DOD Medicare-Eligible Retiree Health Care Fund	188,664	176,113
SSA: Federal Disability Insurance Trust Fund	100,791	132,345
HHS: Federal Supplementary Medical Insurance Trust Fund	67,385	69,324
DOE: Nuclear Waste Disposal Fund	50,598	49,552
OPM: Postal Service Retiree Health Benefits Fund	42,324	45,347
OPM: Employees Life Insurance Fund	41,951	41,250
FDIC: The Deposit Insurance Fund	36,864	36,498
DOL: Unemployment Trust Fund	29,478	20,673
OPM: Employees Health Benefits Fund	23,427	21,259
Treasury: Exchange Stabilization Fund	22,669	22,680
DOL: Pension Benefit Guaranty Corporation	22,575 *	21,114 *
DOS: Foreign Service Retirement and Disability Fund	17,364	16,893
DOT: Airport and Airway Trust Fund	11,808	10,425
NCUA: National Credit Union Share Insurance Fund	10,643	10,297
Other Programs and Funds	92,477	104,409
Total Intragovernmental Debt Holdings	<u>\$ 4,755,715</u>	<u>\$4,789,051</u>

\* These amounts consist of \$4,883 million and \$5,038 million of marketable Treasury securities as well as \$17,692 million and \$16,076 million of GAS securities as of September 30, 2013 and 2012, respectively.

Social Security Administration (SSA); Office of Personnel Management (OPM); Department of Defense (DOD); Department of Health and Human Services (HHS); Department of Energy (DOE); Federal Deposit Insurance Corporation (FDIC); Department of Labor (DOL); Department of the Treasury (Treasury); Department of State (DOS); Department of Transportation (DOT); National Credit Union Administration (NCUA).

*Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service  
For the Fiscal Years Ended September 30, 2013 and 2012*

*(Dollars in Millions)*

**Note 3. Intragovernmental Debt Holdings (continued)**

Intragovernmental Debt Holdings primarily consist of GAS securities. Treasury issues GAS securities at either par value or at an amount that reflects a discount or a premium. GAS securities are issued with a term of on demand out to 30 years. GAS securities include TIPS, which are reported at an inflation-adjusted principal balance using the Consumer Price Index for all Urban Consumers. As of September 30, 2013 and 2012, the inflation-adjusted principal balance included inflation of \$108,908 million and \$96,075 million, respectively. The average interest rates on Intragovernmental Debt Holdings, excluding TIPS, for fiscal years 2013 and 2012 were 3.6 and 3.7 percent, respectively. The average interest rates on TIPS for fiscal years 2013 and 2012 were 1.3 and 1.5 percent, respectively. The average interest rate represents the original issue weighted effective yield on securities outstanding as of September 30, 2013 and 2012.

Fiscal year-end September 30, 2012, occurred on a Sunday. As a result, \$2,145 million of GAS securities held by federal government accounts matured but not repaid is included in the balance of the Intragovernmental Debt Holdings as of September 30, 2012. Settlement of this debt repayment occurred on Monday, October 1, 2012.

**Note 4. Interest Expense**

Interest expense on federal debt for fiscal years 2013 and 2012 consisted of the following:

	<u>2013</u>	<u>2012</u>
Federal Debt Held by the Public		
Accrued Interest	\$242,689	\$240,097
Net Amortization of Premiums and Discounts	4,893	5,318
	<u>247,582</u>	<u>245,415</u>
Intragovernmental Debt Holdings		
Accrued Interest	185,437	191,656
Net Amortization of Premiums and Discounts	(7,807)	(4,616)
	<u>177,630</u>	<u>187,040</u>
Total Interest Expense on Federal Debt Managed by Fiscal Service	<u>\$425,212</u>	<u>\$432,455</u>

The valuation of TIPS is adjusted daily over the life of the security based on the Consumer Price Index for all Urban Consumers. This daily adjustment is an interest expense for federal debt managed by Fiscal Service. Accrued interest on Federal Debt Held by the Public includes inflation adjustments of \$16,548 million and \$10,652 million for fiscal years 2013 and 2012, respectively. Accrued interest on Intragovernmental Debt Holdings includes inflation adjustments of \$10,754 million and \$7,160 million for fiscal years 2013 and 2012, respectively.

*Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service  
For the Fiscal Years Ended September 30, 2013 and 2012*

*(Dollars in Millions)*

**Note 5. Fund Balance with Treasury**

	<u>As of September 30, 2013</u>	<u>As of September 30, 2012</u>
Appropriated Funds Obligated	\$56	\$98

The Fund Balance with Treasury, a non-entity, intragovernmental account, is not included on the Schedules of Federal Debt and is presented for informational purposes.

**Note 6. Subsequent Events**

A delay in raising the statutory debt limit existed as of September 30, 2013. When delays in raising the statutory debt limit occur, Treasury often must deviate from its normal debt management operations and take a number of extraordinary actions to meet the government's obligations as they come due without exceeding the debt limit. Many extraordinary actions taken by Treasury during the period of May 20, 2013 through September 30, 2013, resulted in federal debt securities not being issued to certain federal government accounts. Consequently, the resulting uninvested principal as of September 30, 2013, totaling \$247,827 million and related interest totaling \$801 million are not reported on the Schedule of Federal Debt. Uninvested principal amounts for the Government Securities Investment Fund (G-Fund), Civil Service Retirement and Disability Fund (CSRDF), and Postal Service Retirees Health Benefits Fund (Postal Benefits Fund) were \$119,880 million, \$123,346 million, and \$4,601 million, respectively, as of September 30, 2013. Additionally, the related interest for the G-Fund, CSRDF, and Postal Benefits Fund that would have been accrued and/or paid during the period of May 20, 2013 through September 30, 2013, would have been \$476 million, \$304 million, and \$21 million, respectively, on September 30, 2013.

On October 1, 2013, the Secretary of the Treasury notified Congress that Treasury had begun using the final extraordinary actions and that these actions would be exhausted no later than October 17, 2013. Under the authority of the Continuing Appropriations Act, 2014 (Public Law No 113-46), the statutory debt limit identified in 31 U.S.C. § 3101(b) will not apply for the period of October 17, 2013 through February 7, 2014. In accordance with this Act, on October 17, 2013, the President submitted a written certification to Congress that, absent a suspension of the limit under 31 U.S.C. § 3101(b), the Secretary of the Treasury would be unable to issue debt to meet existing commitments. On October 17, 2013, Treasury discontinued its use of the extraordinary actions and resumed normal debt management operations. On this date, in accordance with relevant laws, Fiscal Service restored uninvested principal amounts to the G-Fund, CSRDF, and Postal Benefits Fund of \$173,948 million, \$117,693 million, and \$4,601 million, respectively. In accordance with relevant laws, Fiscal Service restored the interest related to the uninvested principal during the period of May 20, 2013 through October 16, 2013, to the G-Fund on October 18, 2013 in the amount of \$653 million. Interest related to the uninvested principal during the period of May 20, 2013 through October 16, 2013, for CSRDF and Postal Benefits Fund will be restored on the next semi-annual interest payment date of December 31, 2013. As of October 17, 2013, these amounts were \$562 million and \$24 million respectively.

The Continuing Appropriations Act, 2014, established a process that may result in an increase of the statutory debt limit on February 8, 2014. This increase will be determined by the change in qualifying federal debt securities outstanding on October 17, 2013 compared to those outstanding on February 8, 2014.

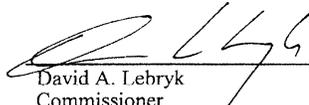
# Appendix I: Management's Report on Internal Control over Financial Reporting Relevant to the Schedule of Federal Debt

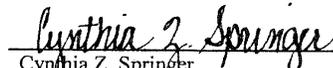
## Management's Report on Internal Control over Financial Reporting Relevant to the Schedule of Federal Debt

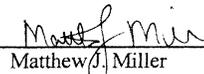
The Bureau of the Fiscal Service's (Fiscal Service) internal control over financial reporting relevant to the Schedule of Federal Debt is a process affected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of the Schedule of Federal Debt in accordance with U.S. generally accepted accounting principles; and (2) transactions related to the Schedule of Federal Debt are executed in accordance with laws governing the use of budget authority and with other applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on the Schedule of Federal Debt.

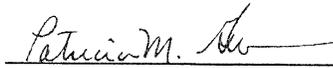
Fiscal Service management is responsible for maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the Schedule of Federal Debt that are free from material misstatement, whether due to fraud or error. Fiscal Service management evaluated the effectiveness of Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2013, based on the criteria established under 31 U.S.C. 3512(c), (d) (commonly known as the Federal Managers' Financial Integrity Act).

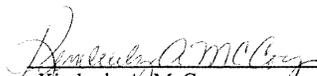
Based on that evaluation, we conclude that, as of September 30, 2013, Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt was effective.

  
\_\_\_\_\_  
David A. Lebryk  
Commissioner  
Bureau of the Fiscal Service

  
\_\_\_\_\_  
Cynthia Z. Springer  
Deputy Commissioner, Fiscal  
Accounting and Shared Services

  
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Matthew J. Miller  
Assistant Commissioner, Fiscal Accounting  
Operations

  
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Patricia M. Greiner  
Chief Financial Officer,  
Assistant Commissioner, Office of  
Management

  
\_\_\_\_\_  
Kimberly A. McCoy  
Chief Information Officer  
Assistant Commissioner, Office of Information  
and Security Services

December 4, 2013

# Appendix II: Comments from the Bureau of the Fiscal Service



DEPARTMENT OF THE TREASURY  
BUREAU OF THE FISCAL SERVICE  
200 THIRD STREET  
PARKERSBURG, WV 26106-5312

December 4, 2013

Mr. Gary T. Engel  
Director, Financial Management and Assurance  
Government Accountability Office  
441 G Street, N.W.  
Washington, DC 20548

Dear Mr. Engel:

This letter is in response to your audit of the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service for the fiscal years ended September 30, 2013 and 2012. We agree with the conclusions of your audit report.

This year was especially challenging as we were faced with two Debt Issuance Suspension Periods (DISPs), the second of which crossed fiscal years. We appreciate the knowledge and experience displayed by your audit team as we encountered unique reporting requirements during these DISPs. Your team's experience with our accounting operations allowed for continued accuracy and consistency as we worked through new accounting scenarios and disclosures. We would like to thank you and your staff for the thorough audit of these schedules as we finalize the seventeenth year of our professional relationship. We look forward to sustaining a productive and successful relationship with your staff.

Sincerely,

A handwritten signature in black ink, appearing to read "D. LeBryk".

David A. LeBryk  
Commissioner  
Bureau of the Fiscal Service

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